

Message Text

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ACTION ABF-01

INFO OCT-01 ISO-00 NEA-10 SP-02 AID-05 EB-07 NSC-05

CIEP-02 TRSE-00 SS-15 STR-04 OMB-01 CEA-01 CIAE-00

COME-00 FRB-01 INR-07 NSAE-00 USIA-15 XMB-04 OPIC-06

LAB-04 SIL-01 L-03 H-02 PA-02 PRS-01 /100 W

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R 150635Z OCT 75

FM AMEMBASSY KATHMANDU

TO SECSTATE WASHDC 3137

INFO AMEMBASSY COLOMBO

AMEMBASSY DACCA

AMEMBASSY ISLAMABAD

AMEMBASSY NEW DELHI

USDEL MTN GENEVA

UNCLAS KATHMANDU 4520

E.O. 11652: N/A

TAGS: EFIN, NP

SUBJ: DEVALUATION OF NEPALESE RUPEE

REF: KATHMANDU 4462

1. THE NEPAL RASTRA BANK HAS ISSUED A STATEMENT EXPLAINING THAT THE PRIMARY MOTIVATION FOR THE DEVALUATION OF THE RUPEE WAS TO ELIMINATE THE ANOMALY IN CROSS RATES VIS-A-VIS THE DOLLAR AND THE INDIA (I.C.) RUPEE. THE NEPALESE (N.C.) RUPEE IS TIED TO BOTH THE DOLLAR AND TO THE INDIAN RUPEE. AS THE STERLING-LINKED I.C. RUPEE PROGRESSIVELY WEAKENED OVER THE PAST YEAR OR SO, THE CROSS-RATE GAP WIDENED UNTIL AT ONE POINT A DOLLAR PURCHASING N.C. VIA INDIA WOULD COMMAND OVER 12.50 RUPEES, AS AGAINST THE DIRECT FIXED RATE OF 10.50. WITH THE INDIAN RUPEE NOW STABILIZED AGAINST A BASKET OF CURRENCIES, THE NEPALESE DEVALUATION HAS RESTORED CROSS-RATE COMPARABILITY, WITH THE N.C. RUPEE WORTH 1.39 TO THE I.C. RUPEE AND 12.45 TO THE DOLLAR. (IT SHOULD BE UNCLASSIFIED

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NOTED THAT THE PROBLEM COULD EASILY RECUR, THOUGH PRESUMABLY

NOT SO DRASTICALLY, SHOULD THE DOLLAR CONTINUE TO STRENGTHEN
AGSAINST THE EUROPEAN CURRENCIES INCLUDED IN THE GOI'S
"BASKET.")

2. THE EFFECT OF THE PREVIOUS CROSS-RATE DISPARITY OF
COURSE WAS THAT ANY PRACTICAL MINDED TOURIST HEADED FOR
NEPAL WOULD PROCUR HIS N.C. RUPEES IN INDIA. (IMPORT
OF N.C. BY TOURISTS IS ILLEGAL, BUT ENFORCEMENT IS
VIRTUALLY NON-EXISTANT.) SMUGGLERS AND BLACK MARKET
OPERATORS ALSO WERE ENJOYING AN EXTRA BENEFIT. IT IS
IMPOSSIBLE TO ESTIMATE THE CUMULATIVE HARD-CURRENCY LOSS
TO THE NEPALESE EXCHECQYER, BUT WITH SOME 80,000 TOURISTS
OVER THE PAST YEAR THE DRAIN COULD EASILY HAVE RUN INTO
SEVERAL MILLIONS OF DOLLAR -- A SIGNIFICANT ELEMENT IN THE
FX RESERVES DRAWDOWN CURRENTLY BEING EXPERIENCED.

3. THE DEVALUATION EFFECT ON NEPAL'S BALANCE OF TRADE
WILL PROBABLY BE ONLY marginally PRODUCTIVE. IMPORT DEMAND
IS RELATIVELY INELASTIC, WITH THE BULK OF IMPORT VOLUME
CONSISTING OF DEVELOPMENT GOODS AND ESSENTIAL CONSUMER
ITEMS. THE STIMULUS TO EXPORTS MAY BE SOMEWHAT GREATER.
PRODUCTION LIMITATIONS RATHER THAN PRICING HAVE BEEN THE
PRIMARY RESTRAINT ON EXPORT GROWTH, BUT INCREASED EXPORT
PROFITABILITY MAY ENCOURAGE GROWTH IN PRODUCTIVE CAPACITY.
THE STIMULUS TO TOURISM SHOULD BE ONE OF THE MAJOR BENEFITS,
ESPECIALLY AS HOTEL SPACE LIMITATIONS BEGIN TO EASE. CARGO

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: RUPEE, DEVALUATIONS, CURRENCIES
Control Number: n/a
Copy: SINGLE
Draft Date: 15 OCT 1975
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: n/a
Disposition Approved on Date:
Disposition Authority: n/a
Disposition Case Number: n/a
Disposition Comment:
Disposition Date: 01 JAN 1960
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1975KATHMA04520
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D750357-0133
From: KATHMANDU
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1975/newtext/t19751052/aaaabucl.tel
Line Count: 87
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION ABF
Original Classification: UNCLASSIFIED
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 2
Previous Channel Indicators: n/a
Previous Classification: n/a
Previous Handling Restrictions: n/a
Reference: 75 KATHMANDU 4462
Review Action: RELEASED, APPROVED
Review Authority: buchant0
Review Comment: n/a
Review Content Flags:
Review Date: 27 OCT 2003
Review Event:
Review Exemptions: n/a
Review History: RELEASED <27 OCT 2003 by MaustMC>; APPROVED <03 FEB 2004 by buchant0>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
06 JUL 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: DEVALUATION OF NEPALESE RUPEE
TAGS: EFIN, NP
To: STATE
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 06 JUL 2006